



GraniteShares' Rhind: Inflation's Peak Improves Prospects For BDCs and CEFs

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Chuck Jaffe, in this episode of The NAVigator podcast interviewed Will Rhind, chief executive officer at GraniteShares, which runs the GraniteShares US High Income ETF. Read the Q&A below as Will says that it appears to him that inflation has peaked and that interest rates are more stable, which has created a more favorable outlook for business-development companies and



closed-end funds. Rhind notes that with economic conditions improving, the prospects for the businesses that are funded by BDCs has become more stable; he also cited the dollar's peak against foreign currencies as improving the prospects for emerging-markets closed-end funds.

Will Rhind

The podcast can be found on AICA's website by clicking here: <https://aicalliance.org/alliance-content/pod-cast/>

CHUCK JAFFE: Will Rhind, chief executive officer at GraniteShares, which runs the GraniteShares US High Income EFT, is here and we're talking about business-development companies and closed-end funds in today's market environment, this is The NAVigator. Welcome to The NAVigator, where we talk about all-weather active investing and plotting a course to financial success with the help of closed-end funds. The NAVigator is brought to you by the Active Investment Company Alliance, a unique industry organization that represents all facets of the closed-end fund industry from users and investors to fund sponsors and creators. If you're looking for excellence beyond indexing, The NAVigator's going to point you in the right direction, and today it brings us in the direction of Will Rhind,

chief executive officer at GraniteShares. Among the firm's funds is the GraniteShares US High Income ETF, ticker symbol HIPS, which offers diversified exposure to MLPs, REITs, real estate investment trusts, business-development companies, and closed-end funds. To learn more go to GraniteShares.com, but to learn more generally about BDCs, interval funds, and closed-end funds go to AICAlliance.org, the website of the Active Investment Company Alliance. Will Rhind, welcome to The NAVigator.

WILL RHIND: Chuck, thank you so much for having me, great to be on.

CHUCK JAFFE: I want to start with a little bit of background on the fund. Investors should know that HIPS is based on the TFMS HIPS Index, so why in working with the index did you combine the four sectors, which is MLPs, BDCs, CEFs, and REITs?

WILL RHIND: Great question. So HIPS is unique really in the sense that it pays a cash distribution, a fixed cash distribution every month, so 10.75 cents per share or \$1.29 of income per annum. And the construction of the portfolio is such that we wanted to create an all-weather income portfolio, so in other words it is able to produce that level of income regardless of whether we've got low growth or high growth in the economy or low inflation or high inflation in the economy. By blending those four sectors together you get an interesting mix, not only are they all passthrough securities of course, they don't pay corporation taxes and therefore the investor starts with a higher level of income, but you mix different income assets together that have different properties. So MLPs for example, which are in the portfolio, will have more exposure to the energy sector versus something like BDCs or REITs which could have exposure to more real estate or mid-sized companies in the US. So by blending those together, the idea is that some part of a portfolio should always be doing well and therefore be able to make that distribution to investors.

CHUCK JAFFE: The other thing about construction that folks want to know is the balance between the asset classes, because right now depending on how you're looking at it you could say, "Well, is the fund performing on par with all of its peers?" And it might be a little bit underperforming, but that could be sector weightings to some extent, so how does that play out?

WILL RHIND: So the way that we do it, first of all, it's equally weighted by sector, so in other words your number of securities. A 60-security portfolio, so you would have 15 securities that are MLPs, 15 that are REITs, 15 that are closed-ends, et cetera. The difference then

becomes we do a minimum variance and optimization which is a volatility control, then decide the actual weighting of those securities, and so right now the portfolio is weighted roughly about 50% to closed-end funds and then the other 50% we've kind of equally split between those other three sectors.

CHUCK JAFFE: For investors who go to check this out, they have lots of reasons just hearing what it does to be interested, and then they're going to go maybe look at some place like Morningstar and see that performance has been very feast or famine. There are times when you're very top of your peer group, very bottom of your peer group on an annualized basis, plus they'll see that the expense ratio is high relative to others, which is why or one reason why Morningstar doesn't give a high star rating and gives a neutral analyst rating. Comment on those things, because I know that obviously you guys had to set the expense ratio, do the rest of that. And I know that you don't entirely believe that when we look any fund this complex through that common, easy, "Hey, it's an easy lens to look at," that it's not necessarily fair to a fund like yours.

WILL RHIND: It's difficult, because as a manufacturer or an issuer one thing that we have to do is we have to create unique or differentiated ETFs. That's how we earn our living, we create value for our customers, that's how we have a business. But sometimes when you do that, and HIPS is a great example of this, where there are no ETFs exactly like HIPS in the market, these websites such as Morningstar, anybody that has to assign a rating puts you in a category. Now their categories are going to be much more generic than allow for something like HIPS, and so it's like literally shoehorning you in a square peg in a round hole from a category perspective. So you could be lumped in a category, as is the case with HIPS, with a bunch of other funds that have nothing to do with the strategy that you have. So with this particular category, whether it's Morningstar or other what I call "stack and rank" websites, you'll get HIPS put into a category of funds that don't do anything like HIPS does, and therefore the performance, the star rating, et cetera, is how you compare to that peer group. But if the peer group is not relevant, then the rating's not going to be relevant, and that's a big issue. The second point is on the expense ratio, the expense ratio looks high and the reason for that is because we as GraniteShares' management company, we charge 70 basis points, 0.7% per annum for the fund. Now the other bit is called acquired fund fees and expenses, so when you look at the expense ratio as the 2.14% for that, that is the majority of

that comes from the BDCs actually. Now even though BDCs are relatively small part of the portfolio, the reason why that shows in the expense ratio is because BDC's are taxed differently than you might expect. They're not taxed as a corporation, they're taxed as a 40 Act mutual fund or registered investment company, and what that means from a tax perspective is you have to declare the expense ratio. And therefore because BDCs support structures more like corporations, in other words they have management teams, they have other expenses, unlike a mutual fund which just supports management fees, you're going to get a higher expense ratio. Now what I always tell people is the amount of money that you're paying for the fund is not actually 2.04% whatever, it's just a function of the way that BDCs are taxed. Now if you look at the tracking error between the ETFs and the underlying index, you'll see that it's about 70 basis points per annum. Which surprise, surprise, that's the fee that we're charging. The other expenses that we have to disclose from a regulatory perspective, they're in the actually securities themselves, and it's really more of a function of the way that BDCs are taxed. Now I know that Congress is trying to change this, a lot of people have a problem with the way that BDCs are taxed, but I think that's probably somewhere in the future that that will actually get changed and it'll be harmonized along with the other investments that we have.

CHUCK JAFFE: I promised that we would be talking about your outlook for closed-end funds and BDCs, and we've spent most of our time doing everything but that so we need to get to that now. Here we are in a time where anything that's producing income, there's a lot of interest in it. We've got changes with what's going on with the Fed, what's happening with inflation and all the rest. So what is your outlook for where BDCs and closed-end funds generally are going? What's going to happen with the discount picture and the rest for this year?

WILL RHIND: I mean, clearly a massive X factor, Chuck, is what does happen with interest rates and inflation? But I think if we were to take the story so far, my outlook for both the asset classes is actually pretty favorable, and the reason for that simply is that if you look at inflation, it looks like inflation broadly speaking has peaked and is on the way down and we've seen the response from the bond market with interest rates drifting down over the last few months as well. Now that obviously doesn't mean that we've absolutely hit a peak in either inflation or in interest rates, but I think it does mean that people are a bit more

confident about the economic outlook than they were certainly six months ago. From that perspective I think that the outlook for both of these asset classes is more favorable. Now I'll obviously have to say that within that it'll depend on the actual strategy for closed-ends, so that's the macro level if you will. The micro level will be, well, what is the actual strategy being deployed by the prospective closed-end fund or BDC? And if you look at, for example in HIPS, top holding that we have in closed-end funds is actually an emerging market closed-end fund. I think in emerging markets for example, that could be a very favorable outlook this year because of the decline in the dollar. So the dollar peaked around August last year and has been on downward trend ever since, and that's good for things like emerging markets. So I think it will depend clearly on the underlying strategy itself and what that particular closed-end or BDC is, but broadly speaking I think economic conditions are actually holding up pretty well. There's some of the credit issues or the outlook for small and medium sized businesses in the US is probably more robust than certainly it was a few months ago.

CHUCK JAFFE: Will, this has been really interesting, thanks so much for joining me on The NAVigator to talk about it.

WILL RHIND: Chuck, my absolute pleasure, thank you so much for having me.

CHUCK JAFFE: The NAVigator is a joint production of the Active Investment Company Alliance and Money Life with Chuck Jaffe. And yes, I am Chuck Jaffe, you can check out my hour-long weekday podcast on your favorite podcast app or by going to MoneyLifeShow.com. To learn more about interval funds, closed-end funds, and business-development companies go to AICAlliance.org, the website for the Active Investment Company Alliance. They're on Facebook and LinkedIn @AICAlliance. Thanks to my guest, Will Rhind, chief executive officer at GraniteShares, which runs HIPS, the GraniteShares US High Income ETF. Learn more about the firm and the fund at GraniteShares.com. The NAVigator podcast is new every Friday, ensure you don't miss an episode by going to where you get the good podcasts and following us there. We'll see you again next week, in the meantime, happy investing everybody.

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